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Before the
FEDERAL COMMUNICATIONS COMMISSION
Washington, DC 20554

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In the Matter of	)	
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Implementation of the Local Competition	)	
Provisions in the Telecommunications Act	)	CC Docket No. 96-98
of 1996	)	

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COMMENTS OF
CONSUMER FEDERATION OF AMERICA (CFA) AND CONSUMERS UNION (CU)

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SUMMARY

THE CONSUMER INTEREST IN COMPETITION IN TELECOMMUNICATIONS

A host of factors prevent competitors from entering the local telephone market. In order to create a level playing field for competition and give the best chance for competition to grow in all segments of the telecommunication industry, barriers to competition in local telephone service must be eliminated quickly, while restrictions on the local monopoly telephone companies are gradually lifted in response to actual changes in the market. Competition is the best form of consumer protection, but premature deregulation is the consumer's worst nightmare, leading to market power disciplined neither by effective competition nor effective regulation.

As a practical matter, residential ratepayers cannot look forward to facilities-based competition on a significant scale in the near to mid-term. No cable company has successfully entered the local exchange market on a significant scale anywhere in the U.S. Long distance carriers have failed in their effort to enter the local market on a wholesale/resale basis. Cellular service remains a very different commodity than basic residential service that has not displaced a significant number of landlines connected and/or local usage.

CFA and CU believe these market realities highlight the importance of implementing pro-competitive, pro-consumer rules with respect to cost allocation and pricing of network elements and services. Our experience in other industries leads us to conclude that policymakers must be extremely careful in establishing the conditions for competition. If we get to a point a few years hence and have alternative regulation and little competition, the Telecommunications Act of 1996 will have been a failure. These comments stress the need for clear national principles to break down the barriers of local monopoly. The FCC should make it clear that competition sooner, rather than latter, is the only acceptable outcome. It should, however, allow the states to determine the precise path to the end point

OPENING THE LOCAL NETWORK TO COMPETITION

The removal of legal barriers to competition is only the first, and in many senses the easiest, step toward competition. Creating the conditions for competition requires providing physical access, operational fairness, and economic feasibility. New entrants must have access to each of the underlying network functionalities at prices that promote efficiency and make entry possible. For over a decade incumbents have resisted the opening of the network and hampered the growth of competition at every turn. The FCC must send a strong message that further delay is unacceptable and the states must move quickly to craft regulations that create the conditions for competitive entry. While the technical and legal conditions are important, the possibility of effective competition will ultimately depend on the pricing principles that regulators adopt.

PRINCIPLES FOR IDENTIFYING COSTS AND SETTING PRICES

Cost causation should be analyzed and defined by the necessary functionalities and capacities projected on a forward-looking basis for those services which are intended to be offered over the network.

(1) Incremental costs for all services should be calculated for the long term on a total service basis (TSLRIC).

(2) Stand-alone costs (SAC) should be calculated on a least cost basis.

(3) The cost methodology should be a bottoms-up methodology consistently applied to the whole, as well as the parts, with costs analyzed consistently across all major services using the same cost methodology and the functionalities or specific capacities having similar costs across services. The same methodology should be applied for costing purposes at retail and wholesale, for bundled and unbundled elements.

Prices should be both efficient and fair.

(4) All users should pay for all functionalities utilized.

(5) Prices should be subsidy free (above TSLRIC and below SAC).

(6) Prices should be based on predictable rules that allocate shared costs across categories in proportion to a measure of cost or use.

The allocation of shared costs should minimize the burden on basic services.

(7) Congress went well beyond a formal definition of cross-subsidy to state a clear preference for cost allocators when it declared that basic service should bear at most a reasonable share of the joint and common costs of facilities used to provide those services

(8) The loop is a joint and common cost - a shared facility that is an input for every service sold in the telecommunications network. Ratepayers do not own the loop and they do not control the incoming calls place on the network by other end-users and service providers.

PRINCIPLES FOR PRICING NETWORK ELEMENTS FOR RESALE ON AN UNBUNDLED OR WHOLESALE BASIS

Competitive entry must be promoted.

(1) Start-up costs associated with the introduction of competition -- e.g. number portability or unbundling and wholesale of network functionalities -- should be

recovered in a competitively neutral manner and not burden specific transactions. Recurring costs associated with sale of monopoly functionalities should be recovered in the price of the services rendered.

(2) Because these are monopoly elements, recovery of costs for shared facilities (contribution) should be no more than what is collected in basic service and contribution should never occur on monopoly elements sold to competitors where it does not occur at retail (i.e. if there are subsidies these need to be "backed out" of unbundled price).

(3) To the extent that universal service funds are created to cover social costs, which are presently included in general contribution, contribution on monopoly elements should be reduced proportionately.

(4) Contribution should be pro rata and fixed. Contribution should be proportionate to elements consumed and not allowed to be shifted to the last kernel of monopoly functionality.

(5) Total wholesale tariffs for basic service should include the same level of basic service contribution as unbundled monopoly functionalities since this competitively neutral with respect to the form of entry (e.g. facilities-based, resale, or wholesale) and supports the policy goal of promoting universal service.

Price and revenue squeezes must be avoided.

(6) If there is any pricing flexibility, the best way to prevent anti-competitive abuse is to set rates without contribution. If pricing flexibility and contribution are both allowed, the imputation standard must be adjusted to reflect discounting, in order to prevent price squeezes. The tariffed rates paid by competitors for network functionalities must be used to calculate the price floor for imputation purposes. If discounts are offered at retail, similar discounts must be automatically passed through to purchasers of the discounted elements at wholesale or a price squeeze is certain.

(7) The purchase of a functionality should allow the purchaser to sell all services associated with those functionalities in the LEC offering. If entrants are not allowed to sell at least the same set of services that the functionality enables LECs to sell, they will be placed at a disadvantage. This is the equivalent of a price squeeze, except it is a revenue squeeze.

PRINCIPLES GOVERNING COMPENSATION FOR INTERCONNECTION

Mutual traffic exchange, which is the current form of interconnection between local companies, promotes economic, technological and administrative efficiency. In this approach companies exchange services (use of facilities) to the maximum extent possible.

1) In an integrated digital telecommunications network efficient routing of calls should take precedence and mutual traffic exchange promotes the use of the technically most efficient path to complete local calls.

2) The FCC should encourage the mutual exchange of traffic to the extent possible and modify that system to prevent gaming, anti-competitive behaviors, or uneconomic outcomes and state commissions should explore mutual traffic exchange, with studies to ascertain whether imbalances will occur in the long term.

3) To the extent that in-kind transactions are deemed inadequate, monetary transactions are necessary, should be based only on imbalances. If usage-based rates are deemed necessary, then they should be applied only to imbalances with compensation at TSLRIC.

4) Reflecting the fact that termination is a monopoly function, if contribution to joint and common costs is allowed, it should be limited to a level similar to that of basic service, as applied to unbundled elements.

PRINCIPLES FOR EVALUATING STRANDED INVESTMENT

Any recovery of stranded investment requires a specific showing of severe economic harms.

(1) There must be a company specific revenue deficiency in the aggregate, a revenue deficiency in the specific exchanges which are said to be creating the social obligation, and the revenue deficiency threatens the financial integrity of the company.

If a company meets the first three tests, regulators should establish procedures to rigorously define uncompensated capital costs associated with "stranded" "obligation to serve investments" including steps to

(2) identify precise assets which are alleged to be "stranded;"

(3) determine whether the assets were deployed to meet an obligation to serve, not a marketing opportunity;

(4) ensure that the assets were the least cost method for discharging the obligation to serve and exclude any imprudence in the investment decision; and

(5) determine the extent to which the risk of the investment being "stranded" has

already been compensated by the risk premium allowed to the utility;

Having rigorously identified the value of the "stranded" investment, regulators should provide for the recovery of those investments in a competitively neutral manner that spreads the burden of the social obligations to all the beneficiaries of that obligation. It should

(6) order the company to write off the value of "stranded" investment;

(7) determine tax benefits of write offs and flow these back through to ratepayers;

(8) seek to recover the maximum amount possible in the disposal of those assets (e.g. offer for sale to the highest bidder or salvage what it can in other ways);

(9) provide for the recovery of remaining costs from a industry-wide recovery fund (probably the universal service fund).

(10) precluded companies from competing in areas in which they have sought "stranded" investment recovery for significant assets for a five year period.

THE COST OF LOCAL SERVICE

Our analysis of cost data suggests LEC claims of embedded costs are grossly out of line with estimates of the cost of the deployment of efficient networks to provide telephone service. The fact that several state commissions have found much lower costs when LEC estimates are subject to careful scrutiny only underscores the unreasonableness of LEC cost claims.
The gap between forward-looking efficient costs and embedded costs can be attributed to a variety of factors for which the incumbent companies have no legitimate basis to claim compensation from ratepayers. These include

(1) misreporting of costs

(2) misallocation of joint and common cost,

(3) excess profits,

(4) inefficiency in design and operation of the network,

(5) strategic investments and

(6) technological obsolescence.

After these costs are excluded, investment that could be "stranded" when regulators impose an efficient pricing policy on interconnection and resale of network elements to promote competition should be subject to the stranded investment recovery principles.

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COMMENTS OF CONSUMER FEDERATION OF AMERICA (CFA) AND CONSUMERS UNION (CU)

The Consumer Federation of America (CFA) and Consumers Union (CU) repectfully submit these initial comments in the above referenced docket.

I. THE CONSUMER INTEREST IN COMPETITION IN TELECOMMUNICATIONS

A. COMPETITION IS THE BEST FORM OF CONSUMER PROTECTION, PREMATURE DEREGULATION IS THE CONSUMER'S WORST ENEMY

In our reply comments in the Universal Service proceeding,[1] we pointed out the important role that competition plays in providing consumer protection under the Telecommunications Act of 1996. We summarized this role as follows.

> Competition plays a key role in both the local company and long distance company arguments. The Inter Exchange Carriers (IXCs) claim that, in the face of competition, neither they, nor the local companies, will be able to impose rate increases on anyone. They claim any cost reductions received will have to be passed-through to consumers because of competition in the long distance market. Further, they say that if regulators adopt sound policies promoting local competition, local rate increases will be avoided.

[1]"Reply Comments of the American Association of Retired Persons, The Consumer Federation of American and Consumers Union," In the Matter of Federal-State Joint Board on Universal Service, Notice of Proposed Rulemaking and Order Establishing Joint Board, Federal Communications Commission, CC Docket No. 96-45, May 7, 1996.

> Local Exchange Companies (LECs) invoke competition in several ways as well. First, they claim that they must rebalance rates because of competition. They claim they can no longer price rural areas and residential service below their costs because competition will attack their urban business customers who are priced above cost. Second, they argue that competition will regulate their ability to increase prices.[2]

We firmly hope that competition in telecommunications will become powerful enough to play this role. Since its inception, the Consumer Federation of America (CFA) and Consumers Union (CU) have vigorously supported competition as the best form of consumer protection. Over the years, however, we have learned that real competition is hard to come by and consumers are ill-served by public policies that simply assume competition will replace monopoly with the wave of a deregulatory wand. Premature deregulation leaves consumers with the worst of all possible worlds, market power disciplined by neither effective competition nor effective regulation.

For almost a decade consumer groups, led by CFA, have been specifying before Congress and state regulators and legislators the conditions and principles that must guide public policy from monopoly to competition in telecommunications. For example, in testimony presented to the En Banc Inquiry on Network Modernization of the New York State Public Service Commission, on September 12, 1991,[3] CFA identified 35 principles for protection of ratepayers, consumers and competition as local networks are opened to competition. These principles have been articulated in more elaborate forms across the country and before Congress

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[2]Reply Comments, p. 20.

[3]Accelerating Deployment of the Intelligent Network: A Telephone Industry Field of Dreams, A Consumer Nightmare, Statement of Dr. Mark N. Cooper.

in the years since.[4] These comments embody a detailed elaboration of those fundamental principles.

The fact that New York was among the first states to move down the path to competition, long before the passage of the 1996 Telecommunications Act, and there is virtually no competition for residential local exchange service available five years later underscores our concern with actual competition in the marketplace.[5] The 1996 Act does not and cannot ensure that competition will actually occur. Even if regulators act quickly and competitors respond aggressively, a monopoly that has existed for over three-quarters of a century is not likely to disappear over night. It may take years, or even decades in some areas, before competition becomes an effective regulator of activity in the local telephone market.

A host of factors prevent competitors from entering the local telephone market. In order

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[4]"Comments of the Consumer Federation of America," In the Matter of a Generic Inquiry by the Commission Into the Plans of the Chesapeake and Potomac Telephone Company of Maryland to Modernize the Telecommunications Infrastructure, Case No. 8388, November 7, 1991; "Statement of Gene Kimmelman, Legislative Director of the Consumer Federation of America on S. 1086, The Telecommunications Act of 1993," before the Communications Subcommittee, United States Senate, September 8, 1993; "Testimony of Dr. Mark N. Cooper, Director of Research of the Consumer Federation of America, on H.R. 3636, the National Communications Competition and Information Infrastructure Act of 1993 and H.R. 3626, the Antitrust Reform Act of 1993 and the Communications Reform Act of 1993," before the Subcommittee on Telecommunications and Finance, Committee on Energy and Commerce, United States House of Representatives, February 3, 1994; "Promoting Competition and Ensuring Consumer Protection on the Information Superhighway: Testimony of Dr. Mark N. Cooper on Behalf of the American Association of Retired Persons and the Consumer Federation of America on Proposed Revisions of Chapter 364," Before the Committee on Commerce and Economic Opportunities, Florida Senate, April 4, 1995.

[5]The situation in New York and elsewhere in introducing local competition illustrates the danger in using a state decision to set national policy as suggested at para. 29 of the Notice. Rather, the FCC should learn from the difficulties faced by the states in their attempts to achieve actual competition.

to create a level playing field for competition and give the best chance for competition to grow in all segments of the telecommunication industry, barriers to competition in local telephone service must be eliminated quickly, while restrictions on the local monopoly telephone companies are gradually lifted in response to actual changes in the market. In order to protect consumers during the transition to competition, regulation over the terms and conditions of services must be maintained until market forces take over.

B. FIRM LEADERSHIP FROM THE FCC MUST BE COMBINED WITH VIGOROUS ACTIONS TO THE STATES TO CREATE EFFECTIVE COMPETITION

For this reason, the Federal law gives the states considerable discretion in how they approach competition and does not require the states to alter the manner in which local exchange service is regulated. We refer to this as pre-emption with a velvet glove. In fact, language which would have explicitly required states to eliminate rate of return regulation was removed from the final bill. As we outlined in our universal service comments to the Joint Board, there is no reason for the transition to competition to lead to rate rebalancing and increased local rates.[6]

The states would do well not to wait too long to get started on the road toward opening up the local market to competition, however. There is nothing to be gained by delay. While the 1996 Act states that competition is national policy, it also says that the states have leeway to implement that policy. Only if states wait and a new entrant complains to the FCC, could

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[6]"Initial Comments of the American Association of Retired Persons, The Consumer Federation of American and Consumers Union," In the Matter of Federal-State Joint Board on Universal Service, Notice of Proposed Rulemaking and Order Establishing Joint Board, Federal Communications Commission, CC Docket No. 96-45, April 12, 1996

a state lose its authority. We are hopeful that many states would begin their proceedings now, set down the rules they think fit their own circumstances and then make minor adjustments after the FCC issues guidelines.

The ultimate goal of the current round of regulation is not regulatory change, it is the promotion of competition. If we get to a point a few years hence with alternative regulation in place and little competition, the telecommunications policy would have been an utter failure for everyone but the local monopoly telephone companies. Our experience in other industries leads us to conclude that policymakers must be extremely careful in establishing the conditions for competition.

These comments will stress the need for clear national principles to break down the barriers of local monopoly as the FCC notes in its tentative conclusion at para. 26 of the Notice. The FCC should make it clear that competition sooner, rather than later, is the only acceptable outcome. It should, however allow the states to determine the precise path to the end point.

To underscore the importance of providing firm leadership in establishing principles for competition, we will review the severe obstacles that local monopolies have created for competition, not only in their long entrenchment in the economic arena, but in their defense of monopoly in the regulatory arena. We believe that this thicket of anti-competitive rhetoric has been cleared away by the new law, but the FCC must not waiver in its resolve to root out the obstacles to competition. While the FCC must make it clear that the anti-competitive weeds must be eliminated; the states should be allowed to choose the means of their extermination.

C. OUTLINE OF THE COMMENTS

Section II of these comments reviews the key barriers to competition which must be removed. CFA and CU identifies the reasons that these barriers are important, the arguments raised by local exchange companies in an attempt to perpetuate them and the steps necessary to remove them. The comments do not delve into the technical details of how the barriers will be removed, however, as these are matters of detail that the competitors will specify through negotiations and the states will implement.

Even with the legal and technical barriers removed, competition will not flourish and consumers will not benefit unless prices are set in a manner that supports entry of competitors. These comments devote the bulk of their attention to pricing matters.

Section III sets out a broad set of general principles to govern pricing.

After this general background is presented, the following sections take up specific issues in pricing for the transition to competition.

Section IV discusses pricing of unbundled network elements.

Section V addresses the issue of pricing access to the bottlenecks.

Section VI addresses the issue of pricing of interconnection.

Section VII address the issue of so-called stranded investment.

Comments then turn to empirical analysis of cost questions.

Section VIII gives a practical example of the concepts and principles by reviewing the debate over cost recovery and cost allocation placed before the FCC in its video dialtone (VDT) proceedings.

Section IX reviews empirical evidence on the actual cost of telephone service on a going forward basis.

II

OPENING THE LOCAL NETWORK TO COMPETITION

A. PHYSICAL, LEGAL AND ECONOMIC BARRIERS TO ENTRY

Exclusive franchises, discriminatory fees, certification procedures, and economic privileges conferred upon the incumbent LECs by legislatures and regulators have rendered competition explicitly illegal in some cases or virtually impossible in others. As long as anti-competitive laws are on the books, competition will not become widespread because legal challenges will be a constant threat.

Just making competition legal may not solve the problem of legal barriers to competitive entry, however. In many states local telephone companies are protected by other statutes that create other barriers, like preventing a competitor from entering a market if that might hurt the financial status of the incumbent local company, imposing fees on competitors at higher rates than incumbents, or establishing certification requirements which make it difficult for entry to take place.

Further, laws, ordinances and contracts put into effect over decades have also given LECs virtually complete control over the rights of way, poles, conduits and entry points that are necessary to deploy a telecommunications network. This makes it difficult for competitors to gain entry.

A century of franchise monopoly status has allowed incumbent LECs to deploy massive amounts of capital equipment in a protected monopoly environment that is economically impossible to replicate by a new entrant in a competitive environment. Because entrants cannot quickly achieve the scale and scope of incumbents, they have difficulty competing.

Monopoly control over virtually all telephone lines, switches and telephone numbers prevents competitors from completing calls on the incumbent's network on terms and conditions that allow them to enter the marketplace. Competitors cannot attract customers if their subscribers cannot reach all telephones on equal technical and economic terms.

The local exchange companies have a ubiquitous network that includes feeder loops with distribution plant (drops) into virtually every residence and business in the country. These loops are connected by trunks to a ubiquitous switching network. Each of these elements (drop, loop, trunking, switching) is a bottleneck or a potential source of insurmountable advantage enjoyed by the incumbent LEC. These bottlenecks and advantages were obtained under an exclusive franchise agreement and a new entrant cannot replicate that network. Competitors must start by serving a small subset or even selective parts of the network both in terms of geographical areas and services. For competition to have an opportunity to develop, the other elements of the network must be available for purchase.

Perhaps the most critical operational problem facing competitors is LEC control over the allocation of telephone numbers. This creates an immense advantage for the incumbent. If potential customers of competitors must change their number to change their local company or dial extra digits to use a competing long distance service the competitors are at a severe disadvantage.

Local exchange companies have been talking about competition for at least a decade, but there is still no effective alternative for local exchange service, particularly residential service. Time and again, the impending, potential technological earthquakes declared by the companies have proven to be false alarms. As a practical matter, residential ratepayers cannot look forward to facilities-based competition on a significant scale in the near to mid-term:

- At present, there would appear to be non-LEC switching capacity capable of providing competition in no more than a few local exchange markets and even that capacity is not being deployed for use in the residential market.

- No cable company has successfully entered the local exchange market on a significant scale anywhere in the U.S.

- Long distance carriers have failed in their effort to enter the local market on a total wholesale resale tariff because of anti-competitive tariffs.

- Cellular service remains a very different commodity than basic residential service. It remains primarily a service for business users and mobile communications. It has not displaced a significant number of landlines connected and/or local usage.

Unfortunately, while facilities-based competition will not develop in the near to mid-term, market structure may be significantly determined in that period. The incumbent LECs are aggressively seeking to reintegrate local and long distance service before there is effective competition for local service. Without unbundling, as well as a total wholesale resale tariff, for network elements and LEC retail services that effectively promotes competition, the incumbent LECs will leverage their unchallengeable monopoly in local service into an artificial advantage in long distance, video and other enhanced services. With that strategic advantage secured, residential customers will see prospects for local competition further reduced and long term, effective competition in long distance and other services undermined.

B. REACTION OF LECS IN THE STATE: FORCING ENTRANTS TO BUILD THEIR OWN NETWORKS

The LECs have taken the position that their control of the existing network creates virtually no barrier to entry. At the state level, they have insisted that mandatory unbundling or resale of piece parts of that network is illegal and unnecessary. They insist that since anyone could build their own network, none of the elements of the current network are bottleneck facilities. Their comments in the Ohio competition proceeding illustrate this point:

> Moreover, no analysis has been conducted as to whether the facilities which are subject to proposed unbundling are essential facilities which cannot be built by competitors. The Staff's proposal does not examine any of the alternatives which are available to other providers, such as self supply, but instead immediately jumped to the unlawful mandatory unbundling requirement.[7]
>
> It is almost the equivalent of saying that those facilities which a given competitor find not in its own self-interest to build are those which can be defined as essential facilities and which the LEC must make available on an unbundled basis. After all, the new entrant can elect to place its own facilities, assuming right of way can be obtained The new entrant can provide its own switching and transport services to customers which it is successful in recruiting; it can extend "loops" to individual customers anywhere it elects to do so.[8]

The company proposals in the states would force entrants to show on a case-by-case basis that each element of the network they seek to purchase from the incumbent is an essential input.

> An "essential input" should capture the circumstances where competing companies of a local exchange carrier do <u>not</u> have economic alternatives sources of an input necessary to produce their competitive service. Criteria based on the nonexistence of the listed conditions should be adequate to apply the basic concept. Any economic alternative source of an input for the relevant market, including self-provisioning that input, is sufficient to determine that input is not "essential".[9]
>
> Furthermore, this make/buy decision will be, of necessity, a situational decision which will vary for a given firm based upon factors such as, but not limited to,

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[7]"Initial Comments of Ameritech, Ohio," before the Public Utilities Commission of Ohio, <u>In the Matter of the Commission Investigation Relative to the Establishment of Local Exchange Competition and Other Competitive Issues,</u> Case No. 95-845-TP-COI, December 14, 1995, p. 57 (hereafter, Ohio Competition Proceeding).

[8]Ohio Competition Proceeding, GTE, p. 9.

[9]Ohio Competition Proceeding, Ameritech, Attachment 2, p. 10.

geography, demography, financial disposition and vendor selection. Add to this the certainty that another firm will arrive at its decision based upon a different mix of the same factors and the permutation of what may constitute "essential" becomes almost entirely subjective. Simply because some firms may find it more efficient to rely on LEC facilities in some cases, is not a reason in and of itself to compel unbundling of existing LEC services.[10]

This approach would create a huge obstacle for entrants. They would never know which elements are available for purchase, since a proceeding would be necessary for them to prove that no alternative is available and it is uneconomic for them to self-supply.

The companies would impose an additional restriction on "pure resellers," proposing that new entrant companies (NECs) who want to engage in resale basically become LECs.

> Discounted resale is a rapid entry alternative and stepping stone to NECs becoming switch based. Discounted resale allows NECs to compete on a wide front, with the option to become switch based as quickly as the NEC chooses. Thus, to qualify for discounted resale NECs should be prepared to meet the same regulatory and social obligations as other local exchange carriers.[11]

In the Ohio case, Ameritech would require that pure resellers purchase services for resale out of end-user tariffs, essentially squeezing them out of the market. Ameritech's proposed restrictions would defeat the purpose of discounted resale, as Ameritech seems to realize.

C. THE PUBLIC POLICY SOLUTION

CFA and CU support the FCC's tentative conclusions at para. 9, 10, and 15 of the Notice. We believe 1996 Act takes some of these arguments away from the incumbent LECs. However, if the FCC does not adopt clear, pro-competitive guidelines in this proceeding,

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[10]Ohio Competition Proceeding, GTE, p. 9.

[11]Ohio Competition Proceeding, Ameritech, p. 71.

competition in the states will be extremely slow to develop.

1. Entry

While it is clear that outright legal barriers to competition must come down, it is equally important to eliminate preferences that have been granted to incumbents. Because of the vast advantage that is enjoyed by the incumbents, even the slightest preference in their favor could doom competition for years to come.

While the terms regulatory symmetry, fairness and equality sound good, they are based on a fundamentally incorrect assumption -- that competitors are equally matched in the marketplace. Incumbent local exchange companies possess all of the advantages inherent in a 75 year old monopoly, while potential entrants do not. Efforts to impose identical regulatory treatment on both, when such large differences in market power exist are doomed to failure. The correct principle is that regulation should be commensurate to actual market power, regardless of who possesses it.

New entrants seeking to provide telecommunications service should be granted a rebuttable presumption that they are non-dominant local exchange companies. The presumption may be rebutted upon a showing that for the particular service(s) in question, a non-dominant competing local carrier has an actual market share within the local exchange company's certificated area that allows it to exercise sufficient control over the market to control prices, or possesses market power in markets which are related to the local exchange service for which the certificate is being sought and is engaging in entry based on anti-competitive or price predatory practices.

The general costs that incumbents claim are associated with implementing the policy of introducing competition (such as costs of developing number portability) must not be placed only on new entrants or their customers, but should be shared by all ratepayers and service providers. Ultimately, all consumers will benefit from competition. It makes little sense to penalize consumers for acting rationally or competitors for being more efficient. It makes even less sense to penalize the most innovative service providers or the most vigorous consumers for being the first to take up competitive alternatives.

Access to public rights of way (streets and buildings) is essential to the deployment of telecommunications infrastructure. Incumbent local exchange companies occupy them at present and local governments or building owners manage them. At the extreme, the LEC may even have powers of eminent domain.

Non-discriminatory access for competitors to the arteries through which the telephone network flows must be ensured on terms and conditions equal to those offered to incumbents. To the extent that rights of way contain excess capacity, this capacity should be made available to incumbents and entrants on an equal footing. Where it is necessary for entrants to rent space in existing rights of way, this should be on terms and conditions which are publicly tariffed and available to all.

While it is understandable that local governments or building owners seek to impose fees or obligations on new entrants which maximized their revenues, it is contrary to the public interest if they treat new entrants differently than the incumbent telephone company. If heavier burdens are imposed on new entrants, which is frequently the case, the result is to place new entrants at a competitive disadvantage.

Ideally, rights of entry for competitors and elimination of preferences for incumbents should be enacted by legislatures. Regardless, the FCC must make certain that in no case should the incumbents receive any legal protections or preferences.

2. Interconnection

The need for interconnection entails a complex set of conditions including: 1) physical interconnection[12]; 2) information in data bases; 3) signalling; 4) technical standards; 5) planning and timing of functionalities; 6) installation; 7) maintenance; 8) testing; and 9) restoration. Non-discriminatory interconnection subject to open technical standards at competitively neutral compensation rates is absolutely necessary to create a competitive local market. Technical standards must not only be made public in advance, but mechanisms for joint determination of standards and protocols must be implemented.

New entrants must not be required to build out a completely duplicative network, either by directly imposing a build out-requirement or indirectly by refusing to make bottleneck facilities available to new entrants under workable terms and conditions. Such a requirement makes little economic sense and is clearly contrary to the public interest. The incumbents have deployed vast amounts of capital and equipment behind a wall of monopoly protection which is virtually impossible to replicate under conditions of competition. Nor is it clear that all facilities should be duplicative. Natural monopoly characteristics may still typify parts of the public switched network, at least in the near and mid-term. Unbundling and resale must be implemented to allow competition to get off the ground. A total wholesale resale tariff may be

[12]This includes physical or virtual co-location. We generally agree with the Notice at para. 67 *et. seq.* that the FCC has the authority to order such collocation and the behavior of the industry suggests that it should do so.

the only way that competitors enter low density segments of the market for a significant period of time.

It is apparent, as a practical matter, that facilities-based competition for residential customers will not be quick to appear on a broad scale. The LECs have once again ignored the fact that they have deployed a ubiquitous interconnected network of billions of dollars of capital assets behind a wall of seventy-five years of monopoly protection. Although the monopoly protections behind which the economic assets were deployed is being slowly dismantled, the economic advantage inherent in the in-place economic assets remains.

Unbundling and resale of the network into its smallest technologically and economically identifiable monopoly components is necessary to allow competitors to purchase bottleneck facilities at non-discriminatory rates without regard to the ultimate use of those components. The purpose of unbundling and resale is to allow entrants to find a technologically and economically manageable set of services to offer in a manageable geographic area. It reduces the scale and scope of operations necessary to enter the market. The series of tentative conclusions found at para. 75-81 of the Notice indicates the FCC recognizes the need to establish national, pro-competitive guidelines that the states will be free to build upon. These policies are absolutely necessary to spur local competition.

CFA supports the FCC's tentative conclusion at para. 57 of the Notice that any unbundling currently being done by a company or required by a state is *de-facto* technically feasible and that the definition of feasibility should evolve along with the network into ever smaller elements. When reviewing the feasibility of a point of interconnection, the burden must be on the incumbent to demonstrate technical infeasibility. It is the incumbent that possesses the best information and the national policy should presume the most pro-competitive outcome.

To the extent that certain elements may be unbundled to facilitate entry, they may be resold, either on a stand alone basis or as part of a package of services. There must be no restrictions set on resale, except that resale across customer classes (i.e. sale of residential services to business customers) should not be permitted.

From the point of view of the entrant, the key to this obligation is non-discriminatory, competitively neutral unbundling of network elements and unrestricted resale of services. From the point of view of the consumer, the key is an effective residential tariff for basic service. The Commission must ensure that entrants do not propose tariffs that effectively preclude residential customers from seeking service with the new entrant.

This requirement is crucial to the transition to competition. It will prevent undue discrimination either within or between customer classes and spreads the benefits of competition to the residential class as quickly as possible.

CFA and CU believe that any concerns about making wholesale prices for LEC services or unbundled elements "too attractive" and thus undermining facilities based competition are totally unfounded. While reasonable pricing is mandatory to allow companies to get a foot-hold in the marketplace quickly, no company wants to rely on its competitor for important elements of their business. Even if the FCC and the states set wholesale and network element prices exactly right, there will be constant pressure on the new entrants to build out facilities.

Many consumers would like the convenience of one-stop shopping for communications services, especially local and long distance. If only one company, the incumbent LEC, is capable of providing this service effectively, it presents a major competitive disadvantage for all